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FEDERAL COMMUNICATIONS COMMISSION  
OFFICE OF THE SECRETARY

Chairman William Kennard  
Office of the Chairman – Eighth Floor  
Federal Communications Commission  
445 12th Street, SW Room  
Washington, D.C. 20554

**RE: AT&T's March 19, 1999 Ex Parte Concerning State UNE Costing Methodologies - Ex Parte Comments:** Two Originals filed in the following docket: *Implementation of the Local Competition Provisions of the Telecommunications Act of 1996* (CC Docket No. 96-98)

Dear Chairman Kennard:

This letter responds generally to AT&T's March 19, 1999, ex parte filing concerning state UNE costing methodologies. We do not address specific state decisions cited by AT&T, which would be more appropriate for direct discussions between the Common Carrier Bureau and the particular state, following the procedures suggested in Part IV, below.

Part I urges the FCC to adopt a "substantial compliance" approach to state costing decisions. Part II emphasizes the need for cooperation and comity between the FCC and state commissions. Part III requests that the FCC abjure results-oriented analyses, and responds to AT&T's use of rank ordering of state results. Part IV concludes by suggesting specific steps the FCC and the state commissions could now take together.

**I. THE FCC SHOULD ADOPT A "SUBSTANTIAL COMPLIANCE" APPROACH TO STATE DECISIONS IN CONNECTION WITH ANY COURT REVIEW OF A STATE'S PRICING METHODOLOGY.**

The FCC authority to establish pricing guidelines was recently reinstated as a result of the recent *Iowa Utilities Board* Supreme Court decision. Since passage of the Act, the States and the FCC have worked together successfully on a broad range of issues. NARUC believes the *Iowa* decision heightens the imperative for continued cooperative FCC- State action.

We appreciate the Commission's past efforts to work closely with the States to facilitate implementation, and look forward to the closer coordination and communication in those efforts the *Iowa* decision requires. With respect to pricing methodologies, at our 1999 Winter Meetings, the NARUC Board of Directors approved a resolution with a simple message:

In keeping with Congress' twin goals of introducing competition for the benefit of the nation's consumers and maintaining universal service, the

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FCC and the States should work together to minimize the prospects for disruption via appeals/collateral attacks upon the myriad of existing State commission pricing orders and related-approved arbitrations that, either (i) specifically comply with the precise text of the original August 1996 order, or (ii) are otherwise in substantial compliance with the FCC's rules."

On March 19, 1999, AT&T filed a position paper on State pricing methodologies. The paper outline's one party's - AT&T - positions with respect to State costing dockets and arbitrations. In many cases, these same positions were argued unsuccessfully to the State commission or on judicial review of the State decision. The paper argues that, "[w]hile a number of states have made significant progress in developing true forward-looking UNE rates, in practice many states...have deviated from the most basic forward-looking cost principles in setting recurring charges, non-recur ring charges, or both." (AT&T Position Paper at page 2). AT&T contends that these "fundamental methodological errors...preclude any general finding that rates adopted by state commissions comply with the [FCC's] pricing rules." (Id. p. 3). As a result, AT&T urges the FCC to "use every opportunity to explain, clarify and elaborate upon its forward-looking pricing rules." (Id. at 22). Thus far, we are pleased that the FCC is taking a cautious approach to addressing State interpretations of the TELRIC methodology. That approach recognizes that State Commissioners, like their federal counterparts, *are public officials sworn to act in the public interest* and, in each of these cases, *are exercising authority in the context of a detailed factual record*.

The States welcome guidance from the FCC on methodological issues. Indeed, if TELRIC is upheld on appeal and one or all fifty States' methodologies are challenged, Courts will no doubt be interested in the FCC's views on whether those State pricing methodologies are sufficiently aligned with the general methodology outlined in the August 1996 order. Whenever the FCC chooses to participate in such challenges, the agency should, where possible, give deference to a State's determinations and find the State is in substantial compliance with the TELRIC methodology.

While we welcome explication of the FCC's pricing rules, we remain concerned that AT&T's approach and criticisms are an effort to draw the FCC into costly, unnecessary and counterproductive micro-management of State pricing decisions and an inappropriate examination of inputs. We urge the FCC not to be swayed by results-oriented analyses of any industry interests, including that offered by AT&T. We believe any FCC action in any proceeding should recognize and respect the decisions of states that made a good-faith, reasoned effort to implement the interconnection provisions of the Act.

## **II. COORDINATION AND COMMITY BETWEEN THE FCC AND THE STATES IS IMPERATIVE.**

The repeated importuning for the FCC to "use every opportunity to explain, clarify, and elaborate upon its forward-looking pricing rules." (Id. at 22) is one of the most troubling aspects of the AT&T paper.

That request is an invitation to a new phase of marketplace uncertainty where States and industry are forced to allocate scarce resources away from issues such as rate de-averaging, rebalancing, intrastate universal service, and other critical proceedings, to argue - after each new clarification - whether the

State's actions comport with the latest FCC pronouncement. There are also legal questions associated with any proposed collateral FCC review of individual State decisions. This would be at odds with the cautious and measured approach suggested by the FCC's actions and statements thus far. Moreover, the resulting proceedings would only hamper overall FCC and State efforts to implement the Act and inject additional uncertainty into the marketplace.

We will not attempt to respond to the specific criticisms of individual State decisions presented by AT&T. If and when such a response is needed, the targeted State is a more expert and appropriate respondent.

We do, however, strongly urge the FCC to defer as much as possible to individual state judgments. This is not to say that States cannot do better or learn from the experience of others. In fact, that is the central benefit of a cooperative, federalist system, which allows for decentralized experimentation with different methods to achieve common goals. Indeed, the August 1996 Order recognizes the benefits of allowing State discretion in implementing the federal interconnection framework: "In this regard, this Order sets minimum, uniform, national rules, but also relies heavily on states to apply these rules and to exercise their own discretion in implementing a pro-competitive regime in their local telephone markets." (First Report and Order, par. 22). AT&T's white paper also largely ignores the effort that States and the FCC have made to work together in implementing the Act. AT&T suggests that there has been a vacuum of FCC guidance and input for the states ever since the 8th Circuit decision, but this clearly is not the case. First, a number of state decisions specifically rely on, or directly quote the August 1996 Order. Second, The FCC was never enjoined from consulting with the states or offering its opinions. To the contrary, States sought FCC guidance. The substantive provisions of the Magna Carta reflect these and related discussions. In part, the Magna Carta declares:

In areas where national standards are appropriate, the FCC will strive to implement them in a way that encourages State and U.S. territory input to the fullest extent possible. The parties recognize the value of diversity and of experimentation in many circumstances. The States and the U.S. territories will support the FCC in its efforts to meet the challenges presented by the implementation of the Act to the fullest extent possible.

So too, each NARUC meeting has included direct FCC-state discussion of particular implementation issues. For example, the NARUC 1998 Winter Meeting included state-FCC workshops on specific topics including "Interconnection Pricing Best Practices - Nonrecurring charges and other issues."

As stated earlier, AT&T's paper is, more than anything else, an invitation to a new phase of litigation, where states and industry participants are forced to expend valuable resources arguing whether the state's pricing rules comply with the Act. In contrast, FCC Chairman Kennard, at the recent NARUC Winter Meeting, urged us all to get beyond litigation at this point and to focus our energies on substantive issues:

What we are living through is truly revolutionary. But, as with any monumental, transforming event, there are differences of opinion about how things should end up and what role each of

us should play. In this case, sometimes our differences have mired us in litigation and distracted us from our real job - serving the American people. For the most part, our differences have not been about where we should end up, but only about how to get there. I feel confident - more confident today than ever before -- that we all deeply share a common bond, borne of our common goal of serving the American people. Our common goal is to serve the American people by fulfilling Congress' goal to bring competition to telecommunications, while preserving our long cherished goals of universal service. We've had our differences about how to get there. But the common goal has always been there. In the wake of last month's Supreme Court decision, it's time to link arms once again and reaffirm our commitment to work together to achieve that goal. It's time for us to make sure that consumers, not lawyers, shape the telecom marketplace. It's time to tell the competitors to take their efforts out of the courtroom and into the marketplace. It's time to move on.

It *is* time to move on. Much work already has been done to implement the Act, but there is much work that still needs to be done. Time spent re-litigating pricing decisions that have been made by the states would not be time well-spent. The FCC should respect the good-faith efforts of the states in implementing the interconnection provisions of the Act, and not accept AT&T's (or any other party's) invitation to more litigation.

### **III. THE FCC SHOULD REJECT RESULTS-ORIENTED ANALYSIS.**

The conclusions and criticisms in AT&T's white paper largely flow from a results-oriented analysis. Such an analysis is inconsistent with the norms for good public policy and administrative agency action. The UNE pricing decisions made by state regulators were (and must) be made on the basis of the evidentiary record developed in each of the state proceedings - not on the basis of comparisons with other state outcomes or even the FCC's proxy ceilings. While AT&T's white paper ostensibly is about general pricing methodology concerns, and not "disagreements about findings of fact and evidence related to cost study inputs" (AT&T paper at 3), the paper describes at length AT&T's criticism of state findings on individual items, which were made on the basis of well-developed record evidence.

In an effort to support its broad conclusions, AT&T appends a results-oriented comparison of state UNE-platform rates with both the FCC's proxy ceilings and a metric of density rank (rank based on the percentage of lines in density zones with over 850 lines per square mile). This effort is flawed in several respects.

First, in terms of the FCC's proxy ceilings, any comparisons must recognize that the FCC developed those proxies to serve as interim prices to be used in the absence of fully-litigated cost studies, not as a measurement tool to judge the reasonableness of fully-litigated cost studies. Indeed, the August

1996 Order recognizes that fully litigated costing studies are innately superior and will likely deviate from the proxies in urging the States to do their own studies." (First Report and Order at paragraph 782.)

Second, in terms of AT&T's density rank comparison to UNE-platform prices, we note the following: Statistically, a perfect one to one correlation is extremely unlikely. However, despite AT&T's assertion, the strong correlation that does exist between density and UNE platform prices suggests that contrary to AT&T's thesis, States did use a generally consistent forward looking costing methodology.

**A. A "perfect" one-to-one statistical relationship between two variables in a complex, multivariate domain of inquiry is extremely unlikely.**

AT&T proposes that the relationship between line density and UNE-P should be perfect. Statistically, it is extremely unlikely two separate variables would have a "perfect" one-to-one statistical relationship. Other variables are at work in determining UNE prices besides the percentage of lines in high density areas. Line density alone does not account for differences in loop costs. Other variables include the population distribution in low density areas and terrain differences. Moreover, information is not presented in the paper to show the rationale behind choosing 850 lines and above as the measure for high density: How might alternative break points affect the analysis? Besides strictly cost-related variables, there were necessary differences in resolving the myriad of interconnection agreements that were negotiated. Each state had different information presented in interconnection proceedings, and had to rely only on the information presented in the record. Many issues were decided besides UNE-P, and trade-offs were achieved that would be equitable to all parties in the proceedings.

**B. However, if one accepts AT&T's analysis, the relationship it demonstrates between density and UNE prices is strong and, in fact, supports the notion that States have used generally consistent forward looking costing methodologies.**

The AT&T data suggests the relationship between population density and UNE prices is strong. However, AT&T presents its results in a way that creates an impression of large aberrations where there is in fact strong consistency.

While it is not a perfect one-to-one correlation, AT&T's data suggests that the relationship between population density and UNE prices is strong. Density appears to be a good surrogate measure for average loop length and to some extent switch size, both of which are substantial cost components of a telephone network. AT&T's results confirm the relationship, as it reports that "the rank coefficient is significantly greater than zero at the 99 percent level of confidence." This shows a very strong association between the two variables. The result is confirmed when you use a standard T-test: The percent of lines in high density areas is strongly related to UNE-P rates, at a 99 percent confidence level.

However, AT&T presents the results of their statistical analysis in a table of comparative rankings. The use of rankings is not dictated by the type of statistical test of correlation that AT&T has

used (a Fisher test), nor would it be appropriate to use a test based on rank order.<sup>1</sup>

A casual reader is likely to pick out rankings for high density lines and UNE prices that are very different. In fact, over half the rankings are within 10 places of each other and 36 out of 46 are within 15 places. Running a T-test on the rankings themselves (rather than the underlying variables) confirms that the two sets of ranks are closely correlated, once again at the 99 percent level of significance. That is, there is a strong statistical relationship between a state's rank on population density and its rank on UNE prices.

#### **IV. THE FCC AND THE STATES SHOULD TAKE STEPS AS PARTNERS TO IMPLEMENT THE FCC'S PRICING RULES.**

NARUC suggests the following steps which should be taken in partnership by the FCC and the states, keeping in mind that under the cooperative federalist system of the Telecommunications Act states are not mere parties before the FCC:

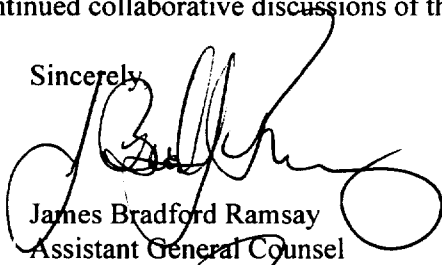
1. NARUC should try to collect State final wholesale pricing orders or their most recent arbitration orders, as appropriate and supply them to the FCC.
2. The Common Carrier Bureau and NARUC should convene a working group of key staff people to identify and address key substantive and procedural issues concerning TELRIC implementation issues on a going forward basis.
3. NARUC should respond to FCC requests for information concerning state wholesale pricing policies.
4. The FCC should appoint a contact for state questions concerning TELRIC implementation.

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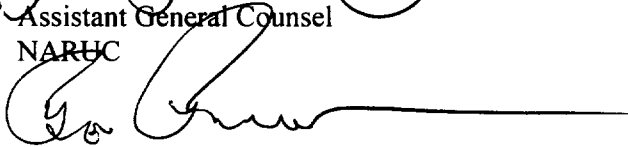
<sup>1</sup> Where the intervals between numbers cannot be assumed to be equal it is appropriate to use a statistical test based on rank order within variables. For example, one person's "strongly approve," scored as a "5" on a psychological test, might not be much different from their "approve," scored as a "4" on the same test. The psychologist should rely on the rank order of responses rather than assume that the intervals between a "5" and a "4" are really "1". For population density, however, four people are exactly "1" different from five people and a nickel is exactly "1" cent more than four cents. For numbers with ratio intervals, like those for population density and prices, a parametric statistic like Fisher's Z-test or a Pearson's T-test is appropriate. For nonparametric statistics, like differences in measures of attitude, a nonparametric test based on rank order, such as a Spearman test, is appropriate.

Again, NARUC reiterates its appreciation for the extreme receptivity and willingness to listen we've received in each FCC Commissioner's office and the Common Carrier Bureau. We look forward to continued collaborative discussions of this and other implementations issues.

Sincerely,

A handwritten signature in black ink, appearing to read "James Ramsay", written over the printed name.

James Bradford Ramsay  
Assistant General Counsel  
NARUC

A handwritten signature in black ink, appearing to read "Bob Rowe", written over the printed name.

Bob Rowe  
Chairman,  
NARUC Telecommunications Committee

## ATTACHMENT A

### AGGREGATE FINAL RESULTS OF NARUC/NRRI SURVEY ON STATE ACTIONS RELATED TO SUPREME COURT DECISION IN AT&T V. IOWA UTILITIES BOARD.

*(44 states responded to the survey as of March 31, 1999)*

1 Adopted geographic deaveraging?

Yes	18
No	21
For some	2
No decision	3

2 If yes, three-zone minimum?

Yes	17
No	1
Some	2

3 Adopted some class-of-service deaveraging?

Yes	1
No	42

4 Procedures and timeframes for filing pre-existing agreements?

Yes	15
No	27
Pending	1

5 Require filing of pre-existing agreements between Class A carriers by 6/30/97?

Yes	13
No	29
Pending	1

6 Any allegation that pricing methodology failed to comply with TELRIC?

Yes	17
No	26

7 Any allegation in a judicial review proceeding that pricing methodology failed to comply with TELRIC?

Yes	14
No	29

8 Beginning of next round of arbitrations?

1999	15
2000	4
Various, including 1999 and 2000	10